

ECONOMICS**November 30, 2018****Brazil Macro Compass****Modest GDP Growth, Confidence Indexes Rise Steeply****Luciano Sobral***

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What's New: GDP Growth and Confidence Indicators

3Q18 GDP growth, as released this week by IBGE, grew 0.8% q/q (+1.3% y/y), in line with our forecast and market consensus. Growth was widespread among the main GDP components: on the supply side, agriculture, industry, and services grew, respectively, 0.7% q/q, 0.4% q/q, and 0.5% q/q. On the demand side, household consumption, the main component, grew 0.6% q/q. Gross fixed capital formation surged 7.8% y/y, but IBGE clarified that imports of machinery related to the oil industry inflated this component (discounting that effect, growth would be 2.7% y/y). It is important to consider that the headline quarterly growth probably overestimates the economic expansion at the margin, considering that 2Q18 growth was hurt by the short-term shock of the May truckers' strike. We believe that the average of the two quarters – 0.5% q/q – is a better reflection of the recent growth rate. We expect 4Q18 growth at 0.6% q/q.

Confidence indicators, according to FGV data, rose steeply in November, in our view probably reflecting the sharp improvement in financial conditions and the conclusion of the electoral process the month before. The consumer confidence and business confidence indexes surged 8.2% m/m and 4.2% m/m, respectively, to new four-year highs. Those moves are, in our view, encouraging signs for consumption and investment in the coming months, aligning with our view that GDP growth will accelerate to 3.2% in 2019.

Political Agenda: Budget and (Still) Transfer of Rights

Next week Congress's joint budget committee is expected to conclude the final steps (the voting of a few sectorial reports remains) needed for the presentation of the final report on 2019 budget, to be submitted to a floor vote before the end of the current legislative year. The deadline imposed by the bill overseer for the incoming government to present amendment requests expired on November 28, with no changes suggested.

The transfer of rights (*cessão onerosa*) bill stalled for another week, with no agreement on the distribution of the associated revenues among the federal government, states, and municipalities and on whether such revenues could be spent without breaching the constitutional spending cap. If there is an agreement, the bill can be submitted to a floor vote next week.

Upcoming Data: November Inflation, October Industrial Production

November CPI inflation will be released on December 7. We expect the index to contract 0.13% m/m, bringing 12-month inflation to 4.13% (from 4.56% in October). The anticipated monthly deflation will be explained by falling fuel prices and electricity tariffs, in our view. Taking that into account, we forecast year-end inflation at 4.0%, comfortably below the 4.5% target midpoint.

On that same day, IBGE also is scheduled to release October industrial production data. We expect 1.5% monthly growth (2.6% y/y), mainly explained by growing auto production and a recovery in oil-related business. It is worth noting that, if confirmed, that growth would interrupt a sequence of three consecutive months of contraction. We believe the growth trend will be confirmed in the following months, as suggested by recently released confidence indicators (see "What's New" above).

IMPORTANT DISCLOSURES/CERTIFICATIONS ARE IN THE "IMPORTANT DISCLOSURES" SECTION OF THIS REPORT.

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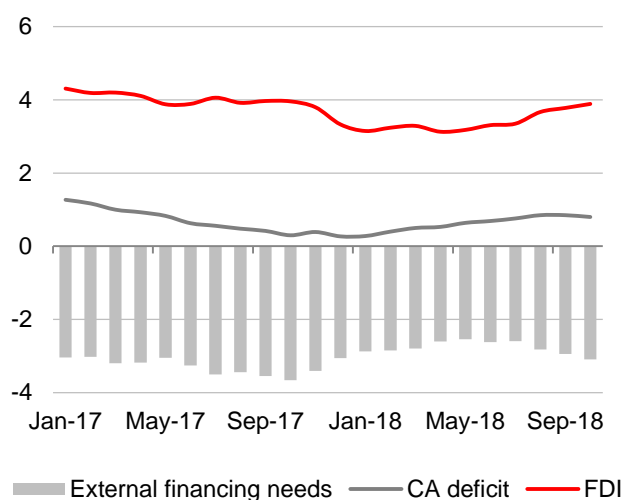
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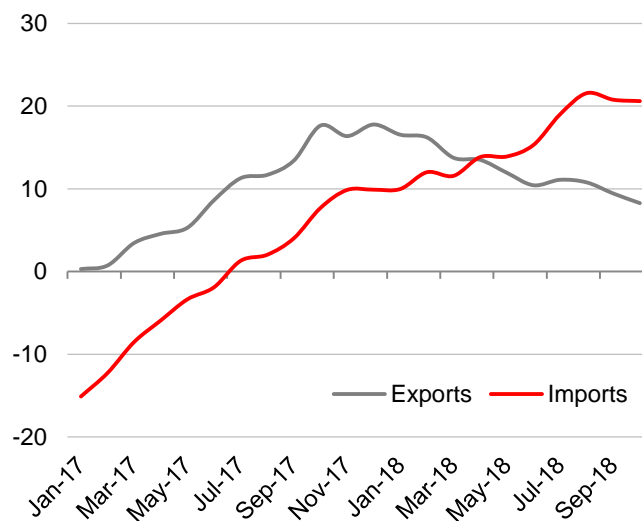
Chart of the Week: Resilient External Sector

October balance of payments data, released this week by the Central Bank, show that Brazil continues to enjoy a comfortable position in external accounts. The country's external financing needs (the difference between the current account deficit and foreign direct investment) were in excess of around 3% of GDP over the past 12 months, helped by a recent acceleration in foreign direct investment. Digging deeper into the data, we found two potential sources of concern: a recent deterioration in the composition of foreign direct investment (the share of intercompany loans in the past 12 months jumped to 24%, from 9% in January) and imports growing at a much stronger pace than exports, leading to deterioration in the trade surplus.

Brazil – External Financing Needs (% of GDP)



12-Month External Trade, Yearly Growth (%)



Sources: Brazil Central Bank, Santander.

Number of the Week

8.2%

According to FGV, consumer confidence jumped 8.2% in November, to a new four-year high. See "What's New" on page 1 of this report.

Quote of the Week

"I think sooner or later Brazil's answer will be inflation again."

— **Carmen Reinhart**, in an interview with *Bloomberg* (November 15, 2018). See "What We've Been Reading" on page 2 of this report.

What We've Been Reading

- "Latin America's New Populism Isn't About the Economy," by Shannon K O'Neil (*Bloomberg Opinion*, November 27, 2018). The failure of judicial institutions to keep up with the trend toward political openness explains the populist wave in Latin America, according to O'Neil.
- "Harvard's Reinhart Sees Rising Risk of Big Emerging-Market Sovereign Defaults," by Ben Bartenstein (*Bloomberg*, November 15, 2018). Reinhart foresees another difficult year for emerging markets in 2019.
- "Rio de Janeiro Elevator Attendants 'Adore' Their Dying, Chatty Trade," by Ernesto Londoño (*The New York Times*, November 25, 2018). A bizarre state law still protects the jobs of thousands of elevator operators in Rio de Janeiro.



Recent Publications (Available on Our Website)

- *Risks for the Selic in 2019 Expected to Become Even Less Asymmetric* (November 6, 2018)
- *20 Charts that Explain Brazil's New Political Power Structure* (October 29, 2018)
- *Brazil Post Elections: Honeymoon and Marriage* (October 25, 2018)
- *Brazil – Risk Premium: Apples and Oranges* (October 9, 2018)
- *BRL: Between Common and Idiosyncratic Factors* (September 26, 2018)



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